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BUY LOCAL PROGRAMS: IMPORT SUBSTITUTION AT THE REGIONAL LEVEL

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Abstract

Import substitution at the local or regional level is a community-based economic inititative that is gaining increasing attention. Import substitution can have a higher multiplier effect on the local economy than export expansion. "Buy-Local" efforts in the state of Oregon, the province of Saskatchewan and the metropolitan area of Victoria, B.C. are reviewed in an effort to establish the principal determinants of, as well as constraints on, a successful regional import substitution program.

BUY-LOCAL PROGRAMS: IMPORT SUBSTITUTION AT THE REGIONAL LEVEL[1]

> ...the all-important function of import-replacing or import substitution is in real life specifically a city function, rather than something a "national economy" can be made to do. (Jane Jacobs, Cities and the Wealth of Nations, p.35.

Introduction

In June, 1984 the Canadian federal government launched a comprehensive national domestic marketing program designed to bring to Canadians an awareness of the benefits of buying domestically produced goods and services. The theme of the program is "Think Canadian" and it includes advertising, public relations, retail promotion and cooperative programs with the private sector to increase consumer awareness of the presence and value of Canadian made products.[2]

In many Canadian communities, however, it is believed that this federal initiative, like so many other federal actions, is too far removed and too uncertain of generating local impacts to be wholly satisfactory. In an effort to create more localized benefits from reorienting expenditures on commodities by local businesses, government agencies and consumers--and in specific cases spurred by the apparent success of the Oregon buy-local program initiated in 1981--regions[3] across Canada are giving

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[1]The author wishes to thank Professors Peter Boothroyd and Brahm Wiesman for their comments on an earlier draft of this paper.
[2]A Gallup survey of 1100 households found that 92% agreed that Canadians should be encouraged to purchase Canadian products. (Canada Commerce 1985).
[3]For purposes of this paper a region is defined as any

increasing attention to import substitution as a locally based strategy for promoting economic development.

Import substitution in this context is said to occur when local purchases of a commodity that is produced outside the region are redirected to a commodity that is produced within. This replacement process directly contributes to local economic development by creating income and employment. The process may contribute also to economic diversity and resiliency.

In the discussion to follow, the impact on the local economy of import substitution is compared with that of the traditionally advocated export expansion. The focus of the comparison is on the economic multiplier effects associated with each. Attention is then directed to existing efforts to promote import substitution by the state of Oregon, the province of Saskatchewan, and the city of Victoria, B.C. In light of these experiences, consideration is given to the essential elements of successful import substitution or buy-local programs and to the potential constraints and costs.

Import Substitution vs Export Expansion

Conventional economic analysis of the export expansion and import substitution multipliers frequently assumes identical effects, i.e. a dollar of increased export sales will have the same impact on the local economy as an additional dollar of local

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[3](cont'd) geographical area smaller than the nation. The terms "regional" and "local" are used interchangeably.

sales attributable to import substitution. For example, Hoover writes

> In the mechanism of the regional export multiplier, expenditures for imports represent demand leakage from the regional stream. The greater the proportion of any increase in regional income that is spent outside the region, the smaller is the multiplier.
>
> It follows that if a region can develop local production to meet a demand previously satisfied by imports, this "*import substitution" will have precisely the same impact upon the regional economy as an equivalent increase in exports*. [emphasis added] In either case, there is an increase in sales by producers within the region.

There is a fundamental confusion here, however, between import substitution and a decrease in imports. A dollar decrease in import purchases will indeed have the same impact on the local economy as a dollar increase in export sales, all other things equal. But a decrease in imports is only half of the process of import substitution. The other half of the process is an increase in local production. A dollar of import substitution (the *replacement* of a dollar of imports by a dollar of local production) will thus have a greater impact on the local economy than will a dollar increase in exports. While it is correct, as Hoover states, that in both cases local production has increased by one dollar, in the case of import substitution, in contrast with export expansion, the local multiplier has been slightly increased.

To illustrate this point in terms of a simple multiplier model, we may first write

$$Y = C + I + G + E - M \tag{1}$$

where

Y = local income	G = government spending
C = consumption	E = exports
I = investment	M = imports

Assuming solely for the purpose of simplifying the exposition that consumption, imports and exports each vary linearly with local income, and that investment and government spending are independent of the level of local income, we may write

$$C = c_0 + c_1 Y \tag{2}$$

$$I = i_0 \tag{3}$$

$$G = g_0 \tag{4}$$

$$M = m_0 + m_1 Y \tag{5}$$

$$E = e_0 + e_1 Y \tag{6}$$

where the subscript $_0$ represents the autonomous (income independent) value of the variable and the subscript $_1$ represents the induced (income dependent) value.

Substitution of (2) through (6) into (1) yields

$$Y = \frac{c_0 + i_0 + g_0 + e_0 - m_0}{1 - c_1 - e_1 + m_1} \tag{7}$$

If it is assumed that exogenous changes in the volumes of exports and imports (i.e. shifts in e_0 and m_0, respectively) result in no, or equal, changes in export and import propensities (e_1 and m_1), then as can be seen from equation (7) a dollar increase in export sales (Δe_0) has precisely the same impact on local income Y as a dollar decrease in import purchases (Δm_0). The multiplier in each case is $1 / (1 - c_1 - e_1 + m_1)$.

In the case of import substitution, however, local production by definition has replaced external production of a particular commodity, thus decreasing the community or regional marginal propensity to import, m_1. The decrease in m_1 in turn increases the value of the multiplier. An increase in import substitution will thus have an arguably greater impact on the local economy than will an equivalent increase in export expansion. Both phenomena increase local production, but import substitution increases the value of the local multiplier as well.

In addition to the stimulus in local production and the increase in the value of the local multiplier that results from the process of import substitution, the process may confer additional benefits on the local economy. For example, import substitution will likely contribute to the diversity of economic activity in the region. This is particularly the case in regions which, through strict adherence to the principle of comparative advantage, have become narrowly specialized in the production of a single or limited number of exportable commodities. An increased diversity of activity is likely to contribute in turn

to the stability of the regional economy, especially if the local activity stimulated or created is not 'forward-linked' (i.e., does not sell intermediate products) to existing export activity. If in the longer run, the local import-replacement activity expands to the point of exporting, it not only generates additional local income and employment, but may make a further contribution to regional economic stability by increasing the diversity of the region's export markets.

To the extent that import substitution results in an expanded range of employment opportunities and to the development of new skills on the part of the local business sector in both services and institutions, the process adds to the economic resiliency of the region. That is, it increases the region's capacity to exploit new opportunities arising from the continuous changes in external economic conditions and to better withstand economic adversity (in that the greater the range of economic activities in the region, the lower will be the probability that all will be simultaneously affected by a downturn).

Some Import Substitution Programs in Practice

The State of Oregon

In January, 1983 a "Buy Oregon" program was initiated by the Neighborhood Economic Development Corporation (NEDCO) in response to a perceived failure of traditional methods of employment creation to replace the jobs that were being lost in Lane County. The objective of the Buy Oregon program was to preserve jobs in

Lane County through import replacement. NEDCO received funding totalling $35,000 from the local public sector (City of Eugene) and private sector (U.S. National Bank's Oregon Economic Action Council and the Lane County Private Industry Council). The program was based on a 1981 study of Lane County businesses, which indicated that the costs of obtaining market information is frequently a significant constraint to business creation and expansion.

> Due to time constraints and traditional methods of purchasing, many firms do not hunt for local suppliers of products they need, often at a considerable cost in freight and storage charges, and in reduced control over quality and service. Local firms can often produce these items at a better price and also provide better service. Moreover, hundreds of local businesses miss lucrative opportunities in their own backyard because they are too young or too small to hire marketing staff. They may be able to offer a high quality product or service needed by another nearby firm, but lack the resources to let others know they exist.

In the first eleven months of the program it was estimated that the initial capital of $35,000 had been leveraged to $1,858,470 through the role of the program as an agent in the creation of direct contracts to local suppliers and direct cost savings to local buyers. Assuming a sales multiplier of 2.5, NEDCO calculated a return of $133 in sales per dollar of initial funding.

The success of the Buy Oregon program led to the creation by the Oregon legislature in 1985 of the Oregon Marketplace (OM), which was conceived as a network of independent import replacement programs throughout the state modeled on the Lane County Buy Oregon program. Each regional program is required to

develop its own plan for structure, operations and long-term financial self-sufficiency. Upon state approval, a regional program is provided with matching funds for up to one year of operation.

The central office in Eugene provides local program staffs with technical training and assistance. The office also maintains a state-wide computer "bulletin board" which contains information on various commodities imported into the State which are deemed to be potentially replaceable by existing local producers or possibly by entrepreneurs wishing to expand their present businesses or create new ones.

The Oregon Marketplace is currently moving into a new phase of development, export expansion. The OM staff recently received a request to "test" the capacity of the network to locate items for export outside the U.S. Some of the initial searches in this context were for chemical-free pet products for export to a country with strong prohibitions against chemicals; petrified wood for use in Japanese ceremonial tea sets; and canned gourmet salmon for international distribution.

The Province of Saskatchewan

For the last three years the Province of Saskatchewan through the Ministry of Tourism and Small Business has sponsored Province-wide competition among local communities in regard to promotional activity on the theme of buying locally. Three population categories have been established--under 400, 400-999

and 1000-5000--and nominal cash prizes are awarded to communities annually for the most novel and effective means of promoting local business.

> Buy Locally Days is a contest for the best promotional campaign by a community on the advantage of buying locally. The contest...is designed to increase public appreciation and patronage of local businesses in villages, towns and organized hamlets. Selection of the winners is based on originality and uniqueness of the events undertaken by the community in promoting Buy Locally Days. (Saskatchewan Urban Municipalities Association 1987)

The competition has generated activities such as "the phantom shopper" who randomly awards silver dollars to patrons of local businesses, essay contests on the need to support local business, art and crafts fairs, junior business ventures in which high school students participate in local business operations and a variety of merchant-sponsored breakfasts and luncheons.

At the provincial level, the Saskatchewan Provincial government in conjunction with the City of Regina, the Purchasing Management Association of Canada (Regina District) and various corporate sponsors has annually sponsored since 1983 a so-called "reverse" trade show.

Trade shows/exhibits have for many decades been organized at various sites to display the products made by various firms and regions. The trade show has traditionally been a broad-scale marketing device to acquaint potential buyers with the range of products offered by the participant exhibitors. As the objective of each exhibitor is to obtain new contracts leading to increased sales. The theme of the typical trade show is export

development. The purpose of the Saskatchewan reverse trade shows, however, is to encourage not export expansion but import replacement.[4] The purpose of the Saskatchewan Manufacturing Opportunites (SMO) shows are not to display Products manufactured in the province but goods and services produced *outside* the Province which are purchased by private sector firms and public sector agencies within the Province. The exhibitors from these organizations place on display imported products that in their judgement may be produced locally. The exhibitors are purchasing personnel rather than sales representatives. Organizers of the SMO argue that the exhibitors

> are most anxious to find suppliers close to home. They know that local manufacturers can offer their in-province customers more personal attention on custom orders and better post-delivery service. Saskatchewan products sold locally often have a competitive edge because their price does not include many of the transportation, duty, exchange and middleman fees associated with imported goods.
>
> Registrants at the show are Saskatchewan manufacturers, suppliers and their sales representatives. They tend to look for new sales opportunities and product development ideas. SMO gives them the opportunity to meet key buyers face to face and discuss sales and manufacturing opportunities in terms of their supply capabilities.(City of Regina 1986, p.1)

Admission to the show is generally gained upon presentation of a business card or by any other means the committee deems appropriate. Each registrant to the SMO is furnished a catalog which lists products purchased by the exhibitors and information regarding annual volumes, prices and/or volumes per individual

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[4] Given recent discussions between Canada and the United States regarding freer trade, the emphasis of promotional efforts regarding the expositions has been on "economic opportunities" rather than "import replacement."

purchase order.

Metropolitan Victoria, B.C.

In April, 1986 a one-day conference was held at the University of Victoria on import substitution at the local level. In attendance were representatives from the Oregon Marketplace, whose success had inspired the formation of the conference, and Vancouver Island mayors, Chambers of Commerce, business leaders and academics. As a direct result of the conference the four municipalities of Greater Victoria (Esquimalt, Saanich, Oak Bay and Victoria) agreed to share with the B.C. Ministry of Economic Development the costs of establishing a buy-local or import substitution program. Approximately four months after the conference had been held, a program manager had been contracted and the "Better-Buy Victoria" program was initiated.

To meet its goals of encouraging import replacement locally and providing an "action model" for community development, the program set forth six strategic objectives:

1. Facilitate business community development within the manufacturing sector;
2. Accumulate information on the local manufacturing sector, current and potential;
3. Identify products with the potential of being locally manufactured by meeting with governmental, institutional and business purchasing agents;
4. Function as a matchmaker (broker) to connect purchasers with manufacturers;
5. Assist local manufacturers to respond to purchasers' needs;
6. Promote the "Buy-Local" idea to the general public and business community to encourage the purchase of locally manufactured products. (Fyfe-Wilson 1987, p. 9-10)

As a first step in an effort to achieve these objectives, contacts were established with individual businesses in the region through information obtained from a variety of sources, including the Provincial government's business data bank, SupplyNet (Province of B.C. 1986). A series of meetings was arranged in which the manager attempted to explain the possible benefits of the program to each potential participant. At the same time a media campaign was launched to inform local consumers of the program's job-creation and retention possibilities.

While the initial response to these efforts was generally positive, a number of negative opinions were expressed. These opinions included the beliefs that:

- local products are of an inferior quality;
- the prices of local products are non-competitive;
- capital constraints would not allow local suppliers to undertake the expansion required to meet import substitution possibilities; and
- shifts to local purchasers may be impeded by head offices;

Three months after the campaign was initiated, however, a survey of 150 businesses in Greater Victoria revealed that that 35% were aware of the program and 93% said they would give preference to local goods and services.

In February, 1987 a Victoria Manufacturers and Producers Association was established with initial financing pledges from over a hundred businesses in the region. The objectives of the Association were to produce a Victoria Manufacturers' Directory and to work with the Better-Buy Victoria program to raise the profile of locally manufactured products.

While it is far too early in the program's development to make any significant judgements regarding the program's overall success, some initial local contracts directly resulting from the program have been reported. These include a $50,000 contract for local t-shirt manufacturing and a $3500 contract for supplying local meat to a community college. In addition, other potential import replacement opportunities have been identified (e.g., the potential of over a million dollars in expanded local production of Victoria school photos and annuals) and there have been organized a number of promotional activities, including a workshop for local fashion designers and manufacturers and a Christmas window display of products from 73 local manufacturers.

Essential Elements of Successful Import Substitution Programs

A cornerstone of a successful import replacement program is an effective core of organizers/directors. Some individual or group must take the initiative for structuring the program and implementing it. Implementation in this case means lobbying and working closely with the local business community. In the case of Oregon's Lane County, the Neighborhood Economic Development Corporation with limited funding from both private and public sources created the import substitution program that later was to expand to the state-wide network of independent local initiatives. In Saskatchewan, the provincial Ministry of Tourism and Small Business promotes buy-local campaigns throughout the province, while the trade shows are organized largely by the Economic Development Department of the City of Regina. The

Victoria Buy-Local program is under the direction of a manager who reports to a board consisting of the Victoria Business and Industrial Development Commission and the provincial Ministry of Economic Development.

A second element in a successful import replacement program is a receptive community. The substitution of local production for imports may be for intermediate products (sales to local businesses) or for final products (sales to local consumers and government). Businesses must be convinced of the potential gains to be derived from such programs.[5] Purchasing agents must see the possibilities of local substitutes with lower prices, higher quality or superior delivery schedules. Producers, and potential producers, must be persuaded of the possibilities of increased sales to the local market. Consumers, as well as local governments, must be convinced of the causal connection of import replacement programs to job creation and of the potential contributions of such programs to economic resiliency, local control of resources and to the future expansion of local exports.

The first two elements are sufficient to identify replacement opportunities within the local economy, should such opportunities exist, but identification alone will not generate increased local economic activity. There must also occur an entrepreneurial response. The local business community must be

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[5]Exploratory efforts in Nanaimo, B.C. regarding the potential benefits of import substitution have met to date with a disappointing response from the local business community. (Ree 1987)

more than cooperative in providing lists and exhibits of purchases; existing and potential producers must take advantage of the opportunities identified. This factor of entrepreneurial response to newly revealed markets deserves particular emphasis. In this context, one might conceptually distinguish three principal categories of regional economies: those in which import-substitution is spontaneously occurring; those in which there is little or no potential for import-substitution; and those in which there is significant but untapped potential for domestic production to replace imported commodities.

Historically import replacement has been, as it continues to be, an unplanned process occurring within many regional economies throughout the world, without the support of buy-local strategies and programs. This would suggest that for such regions programs at the local level designed to foster import replacement may be redundant, merely duplicating the efforts of local entrepreneurs, who both identify and respond to economic opportunities. At the other extreme are those regions in which the potential for import substitution is severely limited. This limitation may in turn be attributed to a lack of a strong local entrepreneurial element, possibly in combination with the lack of replacement opportunities due, say, to a limited supply of natural resources or to the dominance of the local economy by chain operations with established channels of purchasing.

Import substitution programs can be useful, however, in those regional economies in which an entrepreneurial capacity is

present but in a latent form, potentially responsive to the stimulus that such programs might provide. The opportunities to which this local entrepreneurial element might respond is in turn likely to be greater the larger is the transportation factor in the determination of the costs of imported commodities, the greater the scope for attaining sufficient economies of scale in the local market to be cost competitive with externally produced commodities, and the inflexiblity of external producers with regard to customizing products, services and delivery schedules to local needs.

One additional factor of importance to the success of a local import-substitution program is conspicuous by its absence from published discussions of such programs: the lack of similar programs in other regions, particular those regions which constitute the export markets of the region in question. Looking at import-substitution at the regional level from a broader perspective, it must be kept in mind that the replacement of an import by local production means that another region has just experienced a decline in its exports. Let us assume, for example two regions A and B each of which exports to, and imports from, the other. Further assume that an import substitution program undertaken in region A has displaced exports from region B. This decrease in export sales in the external region B can unfavorably affect region A, the import replacing region, in at least two ways. First, there are adverse effects generated through interregional trade linkages. The decline in export sales translates into lower regional income in B which in turn implies

lower consumption by B of imports as well as locally produced commodities. This decline in import purchases by B is likely to mean decreased exports from A. Thus the more significant is the import substitution in a region, the greater is the potentially adverse interregional feedback.[6]

A second possible reaction in external region B that results in negative implications for region A is the initiation by B of its own import substitution program. Region B may adopt such a program in economic retaliation or possibly simply to imitate the success of the existing program in A. In either case, the ultimate effect of B's import replacement efforts (and those of similar efforts in other external regions) may well be a decrease in region A's exports, thus offsetting to some degree any economic gains A initially achieved through its buy-local program.[7]

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[6]To the extent, of course, that import substitution raises income in region A, thus inducing imports which in turn increases the incomes and imports of other regions, A's exports may be increased, partially offsetting the negative interregional impact.

[7]Regions A and B both immediately benefit when resources in A are transferred into more productive activities which: 1) serve the local market without displacing existing local production or imports from B; and 2) are exported to B without displacing B's local production. In the longer run, both A and B may benefit from displacing activities if the response is to shift the resources displaced into one or both of the above activities.

Summary and Conclusions

Import substitution or "buy-Local" programs have been gaining popularity in recent years due in part to the rise of community interests in constructing local initiatives to promote economic development. The success of the program in Lane County Oregon and the Buy Oregon program have given added impetus to the initiation of similar efforts in Canada as well as in the U.S.

While a dollar decrease in imports has the same impact on the local economy as a dollar increase in exports, all other things equal, a dollar increase in import substitution has a somewhat greater economic effect through the alteration of the community's propensity to consume locally supplied commodities. Further, import replacement potentially benefits the community in the long run by contributing to economic diversity which may in turn promote increased economic stability and resiliency, by increasing local ownership of resources which may in turn contribute to a greater measure of control by the community over its economic fortunes, and by adding to local production which may later lead to increased exports.

From a selective review of existing import substitution programs, it may be tentatively concluded that the ingredients for a successful import replacement program are an active and knowledgeable core of organizers and directors of the program, a business community which is receptive to the idea of identifying imported inputs which might be locally supplied, and an entrepreneurial element within the local community which will

capitalize on opportunities identified.

It is further arguable that entrepreneurship is a critical factor. If local businessmen are continuously seeking and exploiting new opportunities, import replacement programs may well be largely superfluous. If, at the other extreme, the local entrepreneurial element is severely limited, no degree of identification of economic opportunities is likely to meet with a response from the commercial sector. In both cases the efforts of those involved in promoting import substitution may be better directed toward other measures to further local economic development.

Finally, it is worth reiterating that from a broader perspective regional import substitution programs approach zero-sum games in their operations. Considered in a multi-regional context, such programs clearly have aspects of a zero sum game. Initially one region's gains in import reductions is another region's loss in export sales. This loss in export revenue can in turn adversely affect the import-replacing region in two ways: through negative interregional trade impacts and through the adoption of import substitution programs in those regions whose exports have been replaced.

In light of the concerns expressed herein, it is advisable for any region considering the initiation of a buy-local program to consider the full potential costs and limitations of such programs as well the possible benefits.

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